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for energy consumers

NGGT, NTS users, interested  
parties and stakeholders

Direct Dial: 020 7901 7159  
Email: andy.burgess@ofgem.gov.uk

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## **Modification of Special Licence Conditions 1A, 2A, 5F, 5G and 11C of National Grid Gas Transporter's Licence to implement Planning and Advanced Reservation of Capacity Agreements**

We are notifying you that we<sup>1</sup> are making changes to the special conditions of National Grid Gas Transmission(NGGT)'s gas transporter licence to allow the introduction of Planning and Advanced Reservation of Capacity Agreements (PARCAs).

The licence modifications will take effect from 31 January 2015.

We issued a statutory consultation<sup>2</sup> and covering letter about our proposed modifications to NGGT's licence on 27 October 2014.<sup>3</sup> These documents explained our reasons for proposing changes to NGGT's licence and sought views from stakeholders. The deadline for representations on the proposed modifications set out in the statutory consultation was 24 November 2014.

The full detail and rationale for these policies can be found in our consultation paper dated 6 August 2014, 'Consultation on changes needed to implement new arrangements for incremental gas transmission capacity (PARCAs)'.<sup>4</sup>

### **Summary of statutory responses and our views**

We received five responses to the statutory consultation. Respondents included NTS users including shippers and developers, NGGT and industry bodies. All the responses were non-confidential and have been published on our website.<sup>5</sup>

Respondents raised points of clarification and provided comments on the licence drafting. The key issues raised were:

- termination costs;

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<sup>1</sup> The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably. The Authority is the Gas and Electricity Markets Authority. Ofgem is the Office of the Gas and Electricity Markets Authority.

<sup>2</sup> Notice under section 23 of the Gas Act 1986 (the Act)

<sup>3</sup> These can be found here: <https://www.ofgem.gov.uk/publications-and-updates/proposed-licence-modification-special-licence-conditions-1a-2a-5f-5g-and-11c-national-grid-gas-transmission%E2%80%99s-licence-implement-planning-and-advanced-reservation-capacity-agreements>

<sup>4</sup> The consultation paper can be found here: <https://www.ofgem.gov.uk/publications-and-updates/consultation-changes-needed-implement-new-arrangements-incremental-gas-transmission-capacity-parcas>

<sup>5</sup> Consultation responses can be found at the link in footnote 2.

- substitution decision timing; and
- further changes proposed to the licence text.

We describe our views, where relevant, on each of these issues below.

You should note that we consulted in June 2014 on changes to Special Condition 1A and 5F of NGGT's licence to facilitate the implementation of the Capacity Allocation Mechanism (CAM) Network Code<sup>6</sup>. The main objective of these changes is to split the Bacton Aggregated System Entry Point into two new virtual entry points. There are no direct policy interactions between the changes in the licence direction implementing the modifications described in this letter and the proposals designed to facilitate the implementation of the CAM Network Code. However, the changes we propose to make in order to implement the CAM Network Code will affect the numbering and cross referencing within both special conditions.

### Termination costs

Four respondents welcomed clarification in the statutory consultation that the costs associated with terminated PARCAs will be subject to the Annual Iteration Process (AIP) assessment. In particular, one respondent said,

*"..assurances that you will scrutinise NGGT costs and the extent to which they have been incurred efficiently and economically provides some comfort that the wider shipper community and customers will not be automatically exposed to expenditure unreasonably and inefficiently incurred by NGGT."*

One respondent referred to our intention to move the text related to the calculation of the PARCA Termination Value in Special Condition 2A to the Price Control Financial Model (PFCM). It said it would work with us to make sure this was complete in time for next year's AIP.

Several respondents suggested that we should have a role in agreeing bilateral contract templates – such as the PARCA contract – between NGGT and industry, and in determining if NGGT has used reasonable endeavours to secure planning permission if a PARCA is terminated.

We have considered the views expressed by respondents. As the process to create the PARCA contract template is outside any framework in which we have a formal decision making role, we have no powers to adjudicate or to determine appropriate contractual terms. We think that National Transmission System (NTS) users and NGGT should have the expertise to determine appropriate contractual terms for agreements that will be signed between both parties.

Nevertheless, we understand respondents' concerns that NGGT may have the ability to impose contractual terms on NTS users. We expect NGGT to engage constructively with its customers to facilitate competitive use of the NTS and inform its business decisions. We would be prepared to have discussions with NTS users if they are concerned this is not happening.

We have attended and contributed to meetings to develop the PARCA contract template. We will continue to feed our views into the development of the contract where appropriate.

The statutory consultation explains our view on assessing NGGT's endeavours in relation to PARCAs that are terminated. We have considered responses to the statutory consultation and maintain our position that the PARCA Applicant and NGGT should have the appropriate legal and planning resources to take this assessment forward.

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<sup>6</sup> Regulation 984/2013 of 14 October 2013 establishing a Network Code on Capacity Allocation Mechanisms in Gas Transmission Systems

## Substitution decision timing

Four respondents expressed concerns about the timing of our substitution decision. The main points made by respondents are -

- NTS users might not make incremental capacity investments if they have to wait until the end of phase two for confirmation of substitution
- the PARCA Security Amount is a form of user commitment
- our substitution decision is an uncontrollable regulatory risk for NTS users
- we should outline the circumstances that would cause us to veto substitution
- vetoing substitution may require the PARCA applicant to go through the planning process again
- exit users may need to take part in the capacity market auction with no guarantee gas capacity will be available.

Similar concerns were expressed in responses to our initial consultation on the proposed PARCA licence changes. We subsequently outlined our position on the timing of our substitution decision in our statutory consultation letter. Having carefully considered the views expressed during the statutory consultation, we consider this decision should be made when the PARCA Applicant is prepared to take on a firm user commitment for the capacity it has requested.

PARCAs have been developed, in part, to delay the need for user commitment until there is certainty that capacity will be delivered. PARCA Applicants who require planning permission will need to put up a PARCA Security Amount<sup>7</sup>. This will demonstrate that the PARCA Applicant is committed to taking the PARCA forward. However, its main purpose is to reimburse NGGT's planning costs if a PARCA is terminated in certain circumstances. We do not consider this is similar to the ongoing user commitment and security requirements NTS users are liable for when capacity is allocated.

In circumstances where planning approval is required, it is only when planning consent is granted that PARCA Applicants will be prepared to take on the appropriate capacity commitments. Until that point, there still remains the risk that a PARCA can be terminated, or the amount of capacity to be delivered changes in response to the planning process. Substitution approval at the end of phase one would not remove these risks.

We said in our statutory consultation letter that safeguards had been built into the PARCA process to make us aware how NGGT intended to deliver capacity through a PARCA. Having carefully considered the views expressed by respondents, we remain of the view that these safeguards are appropriate. If we have concerns about NGGT's proposals, including capacity substitution, we will make them known.

We also made it clear that our position on substitution was based on NGGT properly following the capacity substitution release methodology. Having carefully considered respondents' views, it is difficult for us to foresee any normal network circumstances that may cause us to veto substitution if the methodology is applied correctly by NGGT, and the amount of substituted capacity does not vary significantly during the planning phase. Every veto decision will be made on a case by case basis, taking into account all of the relevant information.

We must also comply with our powers and duties in the Act and in relevant legislation. NTS users should be assured that decisions we make on substitution are bound by this framework, which safeguards industry and consumers against the risk of unreasonable decisions.

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<sup>7</sup> As defined in the UNC.

We decide whether to approve capacity substitution in response to a request from NGGT. We have not proposed any licence changes which amend this requirement. We also consider it would be inappropriate to change the licence to specify a point in the PARCA process when substitution requests should be submitted to us.

If NTS users want this request to be submitted at a particular point in the PARCA process, changes would need to be made to the Uniform Network Code (UNC). The proposed UNC modifications<sup>8</sup> submitted to codify the PARCA process do not include a reference to when NGGT should submit substitution requests to us. We have considered both and chosen to implement the one we think better facilitates the relevant UNC objectives.

The industry can consider and develop further UNC changes to improve the PARCA process through the established modification processes.

#### Proposed licence modifications - Licence text issues

One respondent suggested several minor changes to the licence text contained in the statutory consultation. These changes were mostly to Special Condition 2A and are summarised below.

#### **Special Condition 2A, paragraph 2A.12:**

- the formula for  $REV_{t-2}$  should include the additional term ' $PTV_{t-2}$ '. This is to ensure  $REV_{t-2}$  is indexed to take account of actual RPI adjustments and calculated consistently with other terms in the Special Condition
- add a definition for ' $PTV_{t-2}$ ' in the list of terms in paragraph 2A.12

#### **Special Condition 2A paragraph 2A.16:**

- deleting a blank line underneath the word "where:"
- indenting the  $\sum_{v_j}$  definition
- indenting the second line of the  $\prod_{r=s}^{t-2} PVF_r$  definition
- capitalising all references to "formula year"
- inserting full stops after each of the definitions
- changing the reference to "year" to "Formula Year" in the fourth definition
- changing the reference to "Relevant Year" to "Formula Year" in the  $TR_t$  definition as Relevant Year is not a defined term.

Having carefully considered these proposed changes to the licence text published in the statutory consultation, we think these are minor changes which correct drafting. They do not affect our policy intent or the effect of the licence modifications, and will ensure that termination costs are calculated correctly.

We have therefore incorporated these changes into the licence text included in the statutory direction. They have been highlighted in yellow formatting.

The respondent also suggested amending paragraph 5G.23 in Special Condition 5G. In particular, that the reference to Table 5 in this paragraph should be changed to Table 6. This change is unrelated to the introduction of the PARCA arrangements.

We will consider if this amendment should be made to paragraph 5G.23. If we decide that it should, we will incorporate it into a subsequent licence consultation.

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<sup>8</sup> These can be found on the Joint Office of Gas Transporters website: <http://www.gasgovernance.co.uk>

## **Our decision**

Having carefully considered the responses to our statutory consultation, we have decided to proceed with the modifications to Special Licence Conditions 1A, 2A, 5F, 5G and 11C of NGGT's licence. The effective date of these modifications is on and from 31 January 2015.

A statutory direction modifying NGGT's licence has today been issued to NGGT. The statutory direction has also been published on our website.

## **Next steps**

Licence holders, trade bodies representing licence holders and Citizens Advice/ Citizens Advice Scotland will have 20 working days to decide (from the first working day after this letter is published) if they want to appeal to the Competition and Markets Authority against any licence modifications. Barring any appeal, the licence modifications will have effect from the relevant dates set out above.

If you have any questions regarding the content of this letter, please contact James Thomson by email at [james.thomson@ofgem.gov.uk](mailto:james.thomson@ofgem.gov.uk) or on 0141 331 6012.

Yours faithfully

**Andrew Burgess**

Associate Partner, Transmission and Distribution Policy